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**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

**Telecommunications Division  
Market Structure Branch**

**RESOLUTION T-16941  
June 16, 2005**

**R E S O L U T I O N**

**Resolution T-16941. SBC California (U-1001-C). In compliance with Ordering Paragraph #9 of D. 04-02-063, Ordering Paragraphs 1, 2, 4 and 5 of D. 04-09-061, and the Commission's directive appearing on page 102 of D. 04-09-061.**

**By Advice Letter No. 25978 Filed on December 22, 2004.**

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**Summary:**

This Resolution finds that SBC California's (SBC) filing submitted pursuant to the Phase 2A (D. 04-02-063) and Phase 2B (D. 04-09-061) final decisions is in compliance with those decisions.

This compliance filing deals with the following issues:

- Amended Intrastate Earnings Monitoring Reports (IEMRs) showing adopted audit adjustments and declaration of an officer of Pacific Bell.
- Up to date California Cost Allocation Manual
- Translation of Pacific Bell Information Systems' (PBIS) and Pacific Bell Network Integration's (PBNI) financial trial balances
- Fluctuation Analysis Process

**Background:**

In Decision (D.) 89-10-031, the Commission adopted an incentive-based regulatory framework (called the new regulatory framework or "NRF") for Pacific Bell (now known as SBC California) and GTE California Incorporated/GTEC (now known as Verizon California Incorporated). D.89-10-031 established a triennial review cycle for NRF. The fourth triennial review commenced in 2001 with an Order Instituting Rulemaking (OIR) 01-09-001 and Order Instituting Investigation (OII) 01-09-002

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(collectively, the “Order”). The Order divided this proceeding into three Phases. Most notably for this resolution, Phase 2 included an audit of SBC.

For Phase 2, the Commission hired Overland Consulting (OCI) to conduct the audit of SBC. OCI audited the years of 1997 through 1999 and issued its report in February 2002 with 72 issues.

On April 24, 2002, the assigned Commissioner issued a ruling that bifurcated Phase 2. The scope of Phase 2A was limited to four of the 72 issues that arose from the TD-managed audit of Pacific Bell. These four issues were (1) pensions, (2) PBOPs, (3) depreciation, and (4) income taxes associated with pensions, PBOPs, and the CHCF-B. The remaining 68 audit issues and all Phase 2 service quality issues were assigned to Phase 2B.

On February 26, 2004, the Commission issued D. 04-02-063, which resolved four issues in Phase 2A. Subsequently on September 23, 2004, the Commission issued D. 04-09-061, which addressed the remaining issues. In both decisions, the Commission directed SBC to submit filings as presented in the Discussion section.

**Notice/Protest:**

SBC states that a copy of the Advice Letter (AL) was mailed to competing and adjacent utilities and/or other utilities and interested parties as requested. In addition, SBC states that a copy of the AL was served on all parties to Rulemaking 01-09-001/Investigation 01-09-002. Notice of Advice Letter No. 25978 was published in the Commission Daily Calendar on January 3, 2005.

ORA filed a protest on January 21, 2005. SBC filed its response to ORA’s protest on January 28, 2005. The positions of both parties are detailed below.

**Discussion:**

SBC filed Advice Letter (AL) No. 25978 on December 22, 2004 in compliance with the following Ordering Paragraphs (OPs) of D. 04-02-063 and D. 04-09-061.

**OP #9 of D. 04-02-063 and OPs #1 and #2 of D. 04-09-061 regarding amended IEMRs and Declaration of Office of Pacific Bell**

OP #9 of D. 04-02-063 states:

9. Within 60 days from the effective date of the Phase 2B decision, Pacific shall file an advice letter that contains (i) amended intrastate financial

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monitoring reports for 1997 and subsequent years that reflect all revisions to Pacific's revenues, expenses, NOI, rate base, and accounting and reporting practices adopted by the Commission in Phases 2A and 2B of this proceeding; (ii) work papers that demonstrate that all of the adopted revisions are properly reflected in the amended financial monitoring reports; and (iii) documentation that demonstrates that Pacific's accounting and reporting practices will henceforth comply with today's Order. The documentation shall include a sworn declaration by an officer of Pacific Bell that (i) Pacific no longer engages in the disallowed accounting and reporting practices, and (ii) Pacific has implemented procedures to ensure that Pacific's accounting and reporting practices will henceforth comply with today's Order.

OPs #1 and #2 of D. 04-09-061 states:

1. Pacific Bell, now known as SBC (Pacific), shall prepare a filing that identifies each of this decision's identified errors and demonstrate that Pacific will correct the identified errors in its financial reporting in a manner consistent with GAAP, or as otherwise directed herein. Pacific shall make this filing, along with supporting documentation, as a compliance Advice Letter filing due no later than 90 days after the effective date of this decision. Consistent with Commission practice regarding IEMR disclosure following an audit, SBC shall report to the Commission the impact of identified errors contained herein, on its IEMR for the period in which the error occurred.
2. Pacific shall make a compliance filing within 90 days of the effective date of this decision listing each finding from this decision that has ongoing effects for its record-keeping, reporting or other activities, and demonstrating that its practices going forward comply with this decision.

Attachment 1 of SBC's Advice Letter filing contains SBC's response to the above three ordering paragraphs. Attachment 1 includes four sections:

- Section A – Amended IEMRs
- Section B – Individual Adjustments
- Section C – IEMR Column Detail
- Section D - Validation Matrices

In addition, Attachment 1 should have contained the sworn declaration by an officer of Pacific Bell as stated in OP #9 of D. 04-02-063. The Telecommunications Division's (TD)

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hard copy of the AL did not appear to have this declaration. However, this page can be found on electronic copy filed by SBC on page 437 of the .pdf file.

After meeting with SBC, TD staff was able to trace the adjustments from starting point IEMRs to revised IEMRs.

In its protest, ORA acknowledges that “the 1997 and 1998 and 1999 amounts relate approximately to Appendix D of the Phase 2A decision and to Appendix A of the Phase 2B Decision.” However, ORA goes on to state that “in order to verify the calculation of adopted IEMR adjustments for post 1999 years (2000, 2001, 2002 and 2003), SBC CA needs to provide additional workpapers showing how the adjusted amount for each issue was calculated.” ORA notes that “D. 04-09-061 directs ORA to commence another SBC CA NRF audit for years 2000-2003.<sup>1</sup> Accordingly, other new issues would likely be identified upon a detailed audit of 2000 and subsequent years.”

SBC takes issue with ORA’s statement and states:

The Commission should reject ORA’s attempt to create controversy and unnecessarily add to the workload of SBC California and the Commission. The work papers SBC California provided in its Advice Letter fully complied with the Commission’s requirement that SBC California provide “work papers that demonstrate that all of the adopted revisions are properly reflected in the amended financial monitoring reports...” and documentation showing “that Pacific will correct the identified errors in its financial reporting in a manner consistent with GAAP, or as otherwise directed...”<sup>2</sup>

While we will accept SBC’s AL portion dealing with OP #9 of D. 04-02-063 and OPs #1 and #2 of D. 04-09-061, we have already directed an audit to cover 2000-2004. Through that audit, ORA may seek to determine whether SBC has correctly applied the adopted audit adjustments to these future years.

**OP #4 of D. 04-09-061 regarding Pacific’s California Cost Allocation Manual and Page 102 of D. 04-09-061 regarding Pacific’s Fluctuation Analysis**

OP #4 of D. 04-09-061 states:

4. In its compliance filing due 90 days after the effective date of this decision, Pacific shall address the audit’s assertions regarding whether

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<sup>1</sup> An Assigned Commissioner Ruling (ACR) issued on December 13, 2004 stated its intention to expand the audit period to cover year 2004.

<sup>2</sup> Response of SBC California (U 1001 C) to the Office of Ratepayer Advocates’ Protest to SBC California’s Advice Letter 25978, January 28, 2005, Page 3

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Pacific's California Cost Allocation Manual is up-to-date, including those related to the information Overland obtained from staff. Overland states that responsible Pacific staff acknowledged the need to update the C-CAM. Pacific's staff also identified certain listings in the CAM that required updating, although Overland found the listings the staff identified to be inadequate. Further, Overland claims Pacific's staff told its auditors that certain aspects of the C-CAM had not been updated since 1996. We will then address the issue in Phase 3B of this proceeding.

In addition, pages 102 – 103 of D. 04-09-061 states:

Pacific testified, to the contrary, that all aspects of the C-CAM were updated in December 2000, and that this update is adequate. We cannot reconcile Pacific's testimony with Overland's representation that Pacific staff informed it that the updates occurred in 1996 and identified areas needing updating. We find Pacific's testimony more credible and therefore reject Overland's recommendation.

In Attachment 2 of SBC's AL, SBC stated in its AL that "the C-CAM was updated in December 2000 to address four areas Overland identified as having deficiencies:

- PI System Descriptions
- Cost Allocation Table
- Pacific Reporting System Flowchart
- Category I and II Lists of Services

SBC attached its most recent version of the C-CAM and noted that the C-CAM was updated in November 2002, July 2003, April 2004 and most recently in December 2004.

Page 102 of D. 04-09-061 states:

We order Pacific to make a compliance filing within 90 days of this decision's effective date explaining in detail its fluctuation analysis process and addressing more specifically the auditors' concerns regarding the lack of specificity or a proper audit trail. In Phase 3B of this proceeding, we will then determine whether Pacific's method requires change.

In Attachment 3 of SBC's A.L., SBC explained its Quarterly Fluctuation Analysis and Monthly Fluctuation Analysis and provided:

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- Fluctuation Analysis report for the year ending December 31, 2003 (primarily excerpts related to SBC California)
- Monthly P87 – Cost Allocation System Trending Analysis Report from December 2003
- Source Trending report from January 2003

In its meeting with SBC, TD staff asked about the monthly fluctuation analysis since OC I and the decision focused on the monthly fluctuations. SBC stated that the monthly fluctuation analysis is not really useful since many transactions are only paid quarterly. SBC's own practice is to rely on quarterly reviews.

ORA cites OP #4 of D. 04-09-061 and states that it "will file its testimony in Phase 3B responding to the Commission's direction to address these issues. Therefore, ORA will continue to review SBC CA's filing. Additional discovery may be necessary to determine whether the C-CAM update requirements are met, and whether SBC CA's fluctuation analysis is adequate."

In rebuttal, SBC states that it "fully met the Commission's requirements, and ORA's assertion about any alleged need for additional discovery should be disregarded."

We will accept SBC's filing as is. However, as stated in the OP #4 and Page 102 of D. 04-09-061, at this time, these two issues (C-CAM and Fluctuation Analysis) are anticipated to be addressed in Phase 3B.

**O.P. #5 of D. 04-09-061 regarding Translation of PBIS' and PBNI's Financial Trial Balances**

OP #5 of D. 04-09-061 states:

5. Pacific shall make a compliance filing within 90 days of the effective date of this decision detailing how it will make more transparent and auditable the process it uses for translating PBIS' and PBNI's financial trial balances to its FR books and IEMR reports. Pacific shall also implement its proposed course of action, with any change(s) the Commission orders.

In the A.L. filing, SBC states:

SBC California has permanently discontinued consolidation the financial results of PBIS and PBNI on SBC California's FR books. Therefore, the financial trial balances of PBIS and PBNI have no effect on SBC California's Intrastate Earnings Monitoring Report (IEMR). As a result, SBC California has permanently discontinued the process of translating

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PBIS and PBNI financial trail balances to SBC California's FR books and it IEMR, making the financial data in the FR books and the IEMR fully transparent and auditable.

With regards to this issue, ORA states "as with other mentioned above, the next NRF audit should verify whether or not SBC CA's statements is accurate that PBIS/PBNI no longer impacts its IEMR reports."

SBC states "despite SBC California's straightforward response to Ordering Paragraph 5, ORA seeks to make it an issue in its audit of SBC California...SBC California's response is accurate and easily verified. There is no need for ORA to make it a subject of its audit of SBC California."

We will accept SBC statements that it has discontinued the process of translating PBIS and PBNI financial trial balances to SBC California's FR books and its IEMR, making financial data in the FR books and the IEMR fully transparent and auditable. We will rely on the next audit review to evaluate whether the financial data in the FR books and the IEMR are fully transparent and auditable as SBC says this is easily verified.

**311 Mailing Of Draft Resolution**

In compliance with P.U. Code section 311 (g), a notice letter was e-mailed or mailed on May 17, 2005 to the parties that this draft resolution is available at the Commission's website <http://www.cpuc.ca.gov> and is available for public comments. In addition, TD informed these parties of the availability of the conformed resolutions at the same website.

No comments were received by the Telecommunications Division.

**Findings**

1. On December 22, 2004, SBC filed A.L. No. 25798 in compliance with D. 04-02-063 and D. 04-09-061.
2. In compliance with OP #9 of D. 04-02-063 and OPs #1 and #2 of D. 04-09-061, SBC filed amended IEMRs, individual adjustments, IEMR column detail, validation matrices and a sworn declaration of an officer of SBC.
3. In compliance with OP #4 of D. 04-09-061, SBC stated that "the C-CAM was updated in December 2000 to address four areas Overland identified as having deficiencies: PI System Descriptions, Cost Allocation Table, Pacific Reporting System Flowchart

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and Category I and II lists of services.

4. SBC also attached its most recent version of the C-CAM and noted that the C-CAM was updated in November 2002, July 2003, April 2004 and most recently in December 2004.
5. In compliance with directive appearing on page 102 of D. 04-09-061 regarding fluctuation analysis, SBC explained its Quarterly Fluctuation Analysis and Monthly Fluctuation Analysis and provided examples of:
  - Fluctuation Analysis report for the year ending December 31, 2003 (primarily excerpts related to SBC California)
  - Monthly P87 – Cost Allocation System Trending Analysis Report from December 2003
  - Source Trending report from January 2003
6. ORA filed a protest on January 21, 2005 and SBC responded to the protest on January 28, 2005.
7. No comments were received by the Telecommunications Division.

**THEREFORE, IT IS ORDERED that:**

1. SBC's compliance filing in A.L. # 25978 is in compliance with D. 04-02-063 and D. 04-09-061.
2. This matter is closed.



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This Resolution is effective today.

I hereby certify that the Public Utilities Commission adopted this Resolution at its regular meeting on June 16, 2005. The following Commissioners approved it:

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STEVE LARSON  
Executive Director